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FISCAL IMPACT STATEMENT

LS 6864
BILL NUMBER: HB 1313

NOTE PREPARED: Jan 4, 2004
BILL AMENDED:

SUBJECT: Tax Credit for New Employee Wages.

FIRST AUTHOR: Rep. Buck
FIRST SPONSOR:

BILL STATUS: As Introduced

FUNDS AFFECTED: X GENERAL
X DEDICATED
FEDERAL

IMPACT: State

Summary of Legislation: The bill provides a tax credit for incremental income tax withholding amounts deposited with the Department of State Revenue for wages paid to a new employee in a taxable year.

Effective Date: July 1, 2004.

Explanation of State Expenditures: The Department of State Revenue (DOR) would incur some administrative expenses relating to the revision of tax forms, instructions, and computer programs to incorporate this credit. These expenses presumably could be absorbed given the DOR's existing budget and resources.

Explanation of State Revenues: The bill would reduce state Adjusted Gross Income (AGI) Tax, Insurance Premiums Tax, and Financial Institutions Tax liabilities of individual and corporate taxpayers that have full-time employees who qualify as a "new employee" (see definition below). The credit is equal to the amount of individual income taxes withheld for a new employee by the taxpayer during a taxable year. The taxpayer may claim the credit each year the taxpayer employs the new employee; or the new employee's successor provided the new employee was promoted by the taxpayer to another job. However, the credit can not be claimed for an employee if the taxpayer claims either an EDGE Credit or the Enterprise Zone Employment Cost Credit for the employee. The tax credit is revenue-neutral provided it is claimed for new jobs that would not have been created in the absence of the credit. However, tax credits generated by underlying or natural job growth would result in a revenue loss to the state. The estimated revenue loss from credits generated by underlying job growth in Indiana is presented in the table below.

Fiscal Year	Revenue Loss
2005	$21.4 M - $37.3 M
2006	$44.6 M - $77.8 M
2007	$77.1 M - $135.0 M
2008	$104.1 M - $183.3 M
2009	$116.9 M - $207.2 M

The estimates assume that taxpayers annually have tax liabilities sufficient to exhaust the credit for each new employee. However, these estimates are probably low since they are based on employment totals reflecting net change in employment (gross job gains minus gross job losses). Since credits could potentially be claimed on each job gained, not just the net increase, the revenue loss from the credit could be much higher. The tax credit could potentially affect collections beginning in FY 2005 if employers adjust their quarterly estimated payments.

The tax credit is nonrefundable and may not be carried forward or carried back. For pass through entities, the credit may be claimed by shareholders, partners, or members in proportion to their distributive income from the pass through entity. The tax credit is equal to the income tax withholdings deposited with the DOR for compensation paid during the taxable year to a "new employee." A "new employee" is defined as an employee working at least 35 hours per week; who was first employed in Indiana by the taxpayer after June 30, 2004; and who is not an "excluded employee." An "excluded employee" is defined as an employee: (1) who performs a job that was previously performed by another employee in Indiana, if the job existed for at least 6 months before hiring the new employee and the preceding employee was not promoted to another job; (2) who was previously employed in Indiana by a related member (person or entity with an ownership interest in the taxpayer) and whose employment was transferred to the taxpayer after January 1, 2004; or (3) who is a relative of the employer or an employee, and has at least a 5% ownership interest in the taxpayer.

Revenue from the AGI Tax on corporations, the Financial Institutions Tax, and the Insurance Premiums Tax is distributed to the state General Fund. The revenue from the AGI Tax on individuals is deposited in the state General Fund (86%) and the Property Tax Replacement Fund (14%). Since the tax credit is effective beginning with withholdings during the second half of tax year 2004, the fiscal impact could potentially begin in FY 2005 if taxpayers adjust their quarterly estimated payments.

Background: The revenue loss estimates are based on employment and wage data from the Bureau of Labor Statistics (BLS). Underlying growth in private employment in Indiana is assumed to range from 1.1% to 1.9% annually. These growth rates reflect long-run trends in private employment levels in Indiana. These rates are also consistent with national projections suggesting average annual growth in employment equal to about 1.4% from 2000 to 2010. Indiana private employment in 2003 totaled about 2.47 M. This total serves as the base employment for estimated employment growth in subsequent years. In addition, job tenure equal to four years is assumed. BLS analysis indicates that nationally employee tenure has been fairly consistent, with the median employee job tenure ranging from 3.5 to 3.8 years since 1996. Quarterly wage data from the BLS indicates that the average annual wage in Indiana was about $33,900 during the 4th quarter of 2002. Annual wage growth of 3.4% is assumed based on long-run trends in the BLS wage data. Taxable income is derived by subtracting the average 2001 total deduction amount (= $1,700) and total exemption amount (=$3,100) from the average wage. Withholdings and, as a result, the tax credit are assumed to equal 3.4%

of new employee taxable income.

Explanation of Local Expenditures:

Explanation of Local Revenues:

State Agencies Affected: Department of State Revenue.

Local Agencies Affected:

Information Sources: U.S. Bureau of Labor Statistics (BLS), www.bls.gov. BLS, *Covered Establishments, Employment, and Wages by State, Preliminary Data, Fourth Quarter 2002*. BLS, *Employee Tenure in 2002.* BLS, *State and Area Employment, Hours and Earnings*. BLS, *Business Employment Dynamics Data.* OFMA Income Tax Database, 2001. BLS, Daniel E. Hecker, Occupational Employment Projections to 2010, November 2001.

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